

Inventory and Self-Employed Taxpayers

If the taxpayer indicates in **Part I** of a **Self-Employment Worksheet** that they maintain an inventory:

1. Ask the taxpayer about the inventory that they keep.
2. Ask them to list the expense of acquiring the “inventory” in the **Supplies** section of the **Self-Employment Worksheet**.
3. Continue with Intake for VITA tax preparation.

These are examples of self-employed taxpayers who may answer that they keep an inventory:

- garage sale/EBay sellers
- self-employed stylists selling hair products

VITA Scope of Service and Inventory

Generally, if a taxpayer produces, purchases, or sells merchandise in their business, they must take “inventories” into account at the beginning and end of any tax year, use the accrual method of accounting for purchases and sales of merchandise, and report inventory costs as **Cost of Goods Sold** on a tax return. The accrual method of accounting for self-employed taxpayers is out of scope for VITA and Special Tax Services does not prepare tax returns that include **Cost of Goods Sold**.

However, an exception exists for small business taxpayers. A taxpayer is considered a small business taxpayer if they have average annual gross receipts of \$26 million or less for the 3 prior tax years and are not a tax shelter. This includes nearly all of the Tax Help Program’s self-employed taxpayers.

Rather than reporting the **Cost of Goods Sold** and using the accrual method of accounting, small business taxpayers using the cash method of accounting (which is in scope for VITA) can choose not to keep an “inventory” and instead account for the goods, merchandise or stock, raw materials, finished products, or supplies that physically become part of an item intended for sale (“inventory”) as “non-incident material or supplies” on their tax return.

If the taxpayer chooses not to account for “inventory” and instead will report inventory expenses as non-incident materials and supplies, the taxpayer can deduct the amounts paid or incurred to acquire or produce the inventoriable items in the year in which they are first used or consumed in the business. This tax return is in scope for VITA and the Tax Help Program.

For more information:

- [Publication 334, Tax Guide for Small Business](#)
- [Pub 4012, VITA/TCE Volunteer Resource Guide](#)